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Will Financial Pressures on YRCW (Yellow Roadway) and other Carriers Ultimately Mean Danger for Shippers

Expansion and Acquisitions in Heady Days Mean Additional Pressures in Transport Slump; How Much Capacity Will Leave the Market

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After heady times in 2004-2006, business for most trucking companies started to slow in 2007, and then has slumped dramatically in recent months as the domestic and global economy cratered.

What will be the ultimate impact to the trucking industry and shippers?

That's hard to say, although it's clear much capacity has already been removed from the market, especially from independent and smaller trucking firms, as demand and rates drooped sharply earlier this year even as fuel costs soared. In May, the American Trucking Associates found that more than 800 trucking firms with at least five vehicles had left the market in Q1 2008, and many believe that number went over 1000 in Q2. That doesn't include sole proprietors that have left the market, and was before the financial crisis and recessionary environment that has reduced freight demand even further.

Those financial pressures are now hitting even the industry's largest carriers hard.

As reported last week by transportation industry analyst **Ed Wolfe** of Wolfe Research, YRWC (Yellow Roadway) is now under significant financial pressure to reduce debt and meet its loan covenants (financial requirements under terms of a loan).

Wolfe reports that YRCW ended the third quarter with a debt to EBIDTA ratio of just 3.2, "dangerously close" to its load covenants that require a maximum ratio of 3.5. Wolfe Research "believes that YRWC is likely to take further action in the near term to reduce debt and avoid a covenant breach," which can lead to various unpleasant consequences.

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What can YRWC do to reduce its debt levels? Without getting too much into the financial minutia. Wolfe says the company can use a revolving bank credit line to retire other bond debt, which would "likely extend its potential covenant breach another 2-3 quarters."

Wolfe says the company may also look to sell assets to raise cash and retire debt, including selling redundant terminals that resulted from the Yellow acquisition of Roadway Express in 2003. Unfortunately, there may be few buyers for those terminals in this environment, a situation made worse by recent market availability of 40 small Con-Way LTL terminals and 300 DHL parcel terminals coming to market.

Is the current YRWC debt load the result of borrowing to fund Yellow's purchases of competitors Roadway and US Freightways?

No and yes, says Wolfe Research's **Tim Denoyer**. "At this point most of YRWC's debt was issued af-

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ter the Roadway merger, so it's difficult to attribute it solely to that," said Denoyer. However, "You could make the argument that they wouldn't be in the current situation had they not paid so much for Roadway and US Freightways. Early this year they wrote down $703M of goodwill and intangibles from US Freightways and $77M for Roadway, and after 3Q they wrote down $636M from Roadway, $89M from USF, and $98M from YRC Logistics, much of which is likely the former USF Logistics. That's a total of $1.6B in impairment of intangible assets and goodwill from both acquisitions (in accounting terms intangibles and goodwill are generally amounts paid for acquired assets above their book values), which is more than YRWC's current debt level."

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